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Retail Food Sector

Park 'N Shop Pulls Out of Shanghai

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Report Highlights:

Following hot on the heels of Dutch retailer Ahold-Tops' pullout from China last summer, Park 'N Shop has decided to depart from the highly competitive Shanghai retail sector, further evidence that cut-throat competition, oversupply, and pressure from the more successful hypermarket format (Carrefour, Metro, Auchon) is taking its toll. Park 'N Shop will retain a management contract with one existing Shanghai store, but will sell the equity in its other local stores to an un-named company.

Includes PSD changes: No
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Shanghai ATO [CH2], CH

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According to industry insiders, there is likely not a single operator in Shanghai's food retail sector which is operating in the black, although some report that Carrefour is the only operator to be making a profit. The competitive pressure puts the foreign firms (which have investment caps placed on their operations by the government) at a competitive disadvantage to their state-run competitors. Although the domestic firms lack technology, sophisticated training, and management know-how, they do have very deep pockets in the form of soft loans from state banks, and vested interests in their respective local governments which view creating jobs as a way of maintaining stability in China's cities. The stronger Chinese firms are also buying up their smaller and less successful domestic competitors, rapidly consolidating an industry which is less than ten years old, but already achieving a penetration of over1200 supermarkets in a single city (Shanghai). Hualian and Lianhua, both state-owned goliaths, have come out the winners in this contest to devour the competition as rapidly as possible. These two chains control more than half of the city's supermarkets, and they have also diversified into convenience stores and hypermarkets.

Another hard reality is that China doesn't really encourage foreign competitors operating in its retail sector. Pending-WTO accession aside, local governments view foreign retailers as both a showcase of technology intended to provide a model for local emulation, and as a threat to domestic retailers. Many foreign ventures have been starved out of existence with red tape, investment caps, weak local partners that are often foisted on the foreign investors, and general interference from the local and central government.

A common local perception is that foreign firms are here to repatriate profits and plunder China's resources. However, in reality, most foreign firms take long-term stakes in China, reinvesting their profits in order to build the business, while their Chinese partners demand short-term profit taking to pay off debts incurred by their parent company, or to pay for social welfare programs unrelated to the workers assigned to the joint venture. Not surprisingly, the overlooked aspect of retailers like Carrefour is that its hugely successful format sells more Chinese goods and pays higher wages to its Chinese workers than do its domestic competitors.

We foresee continued consolidation in the glutted food retail sector, and also many local competitors entering into the hypermarket format in the coming 2-3 years.